



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

NO PROTEST RECEIVED
Release to Manager, NO Determinations - Cincinnati

DATE: [REDACTED]

SURNAME [REDACTED]

Date: [REDACTED]

Contact Person: [REDACTED]

Identification Number: [REDACTED]

Contact Number: [REDACTED]

Employer Identification Number: [REDACTED]

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(7). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

You were formed on [REDACTED], under the [REDACTED] Article II of your Articles of Organization states that your purpose or purposes "is to engage in any activity within the purposes for which a limited liability company may be formed" under the Michigan statute.

Your other formative document is an Operating Statement/Agreement, which is dated [REDACTED]. The opening paragraph of this document identifies the four individuals who have entered into the Operating Agreement, who are referred to as "Member" or "Members". They each have received Certificates of Membership (see Article 1, Sec. 1.6) and each Member has made a Capital Contribution of \$[REDACTED], which represents a "Sharing Ratio" of [REDACTED]% (see Exhibit A, an attachment to the Operating Agreement).

Article 2, Sec. 2.2, entitled Capital Accounts, states, in part, that "The capital account of each Member shall be credited with his capital contribution(s) (at net fair market value with respect to any contributed property) and shall be appropriately adjusted to reflect each Member's allocation of profits, gains, losses, deductions, the net fair market value of distributions made to the Member(s), and any other adjustments as required by section 704(b) of the Internal Revenue Code...."

Article 3, Sec. 3.1, provides that the Company's net profits or net losses shall be determined on an annual basis and shall be allocated to the Member(s) in proportion to their Sharing Ratios.

[REDACTED]

Article 4, Sec. 4.1 provides that the business affairs of the Company shall be managed by the Members in proportion to their Sharing Ratios.

Article 5 sets forth the rules for the transfer of a "Company Interest" by a Member. Sec. 5.1 allows for the transfer of such interest to a Trust, as long as the Member acts as the initial Trustee and grantor of said Trust. The "Holder" of such interest can include a Member, an estate, a trust, a bankruptcy trustee, a receiver, etc.

In response to Part II, 1, of Form 1024, exemption application, you describe yourself as a "social organization" formed by your members to purchase land for purposes of outdoor recreation. Outdoor recreation activities include hunting, fishing, and camping.

In a letter dated [REDACTED], you have responded to our development letter of [REDACTED]. In Response #2, you describe the property which you purchased from [REDACTED] on [REDACTED] (in the amount of \$[REDACTED]). The property consists of 40 acres located approximately [REDACTED]. The property is made up of [REDACTED] percent hardwood forest and [REDACTED] percent densely forested [REDACTED]. To date, the only improvements "have been an eight by ten foot wooden storage shed and a four by four wooden outhouse." You represent that the sole purpose for the purchase of this property is for "recreational uses, hunting, fishing, camping, and small social gatherings."

In #3, we inquired as to how often your members met and requested details concerning any social commingling among your members. You responded, in part, that your four identified members meet twice a year, in the spring and fall. You did not provide any information concerning any social commingling among your members in the context of your organization's activities.

In response #5, you reported total income of \$[REDACTED] for your taxable year ending [REDACTED]. Your reported expenses totaled \$[REDACTED] consisting of mortgage payments of \$[REDACTED], property tax of \$[REDACTED], and outlays of \$[REDACTED] for a storage shed and \$[REDACTED] for the outhouse. The resulting balance for this taxable year was \$[REDACTED].

Section 501(c)(7) of the Internal Revenue Code provides for the exemption from federal income tax of clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, substantially all the activities of which are for such purposes and no part of the net earnings of which inures to the benefit of any private shareholder.

Section 1.501(a)-1(c) of the Income Tax Regulations provides that the term "private shareholders or individuals" refers to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(7)-1(a) of the regulations essentially repeats the language of Code section 501(c)(7) but also states that, in general, this exemption extends to social and recreation clubs which are supported solely by membership fees, dues, and assessments. However, a club otherwise entitled to exemption will not be disqualified because it raises revenue from members through the use of club facilities or in connection with club activities.

[REDACTED]

Rev. Rul. 58-589, 1958-2 C.B. 266, discusses the various criteria for recognition of exemption under section 501(c)(7) of the Code. In order to establish that a club is organized and operated for pleasure, recreation, and other nonproftable purposes, "there must be an established membership of individuals, personal contacts and fellowship. A commingling of the members must play a material part in the life of the organization."

Rev. Rul. 70-32, 1970-1 C.B. 132, describes a club organized to own and operate aircraft suitable for business or personal use by its members, to enable its members to improve their flying abilities, and, through the ownership and maintenance of flying equipment, to provide economic flying facilities for its members. Membership is open to all persons who are interested in flying.

Rev. Rul. 70-32 cites Code section 501(c)(7) and states that in order for a club to qualify for exemption under this section, "there must be an established membership of individuals, personal contacts, and fellowship. Furthermore, a commingling of members must play a material part in the activities of the organization." Rev. Rul. 58-589, 1958-2 C.B. 266 and Rev. Rul. 69-535, 1969-2 C.B. 126 are cited.

Held, the above-described club does not qualify for exemption under Code section 501(c)(7) because its sole activity is rendering flying services to its members and there is no significant commingling of its members.

With respect to your application, we note that your creating instrument makes no mention of any recreational or social purposes. Instead, you were essentially formed for business purposes. If your purposes were otherwise, you could have opted to be organized under the nonprofit statute of [REDACTED] rather than as an LLC. The indication of an overriding business purpose is reinforced by the language in your Operating Agreement, which spells out at considerable length the financial obligations and contractual powers of your Members. Further, each of your four Members has a [REDACTED] percent share in the principal and income, and profits and losses, of the LLC. This provision directly contravenes the requirement, under Code section 501(c)(7), that no part of the net earnings of a club may inure to the benefit of any private shareholder. Your four Members are clearly "private shareholders" per the definition in section 1.501(a)-1(c) of the regulations.

Aside from the organizational defects noted above, we also conclude that you do not meet the requirements of Code section 501(c)(7) because the required commingling among your membership does not exist to any significant degree. See the holdings in Rev. Ruls. 58-589 and 70-32, discussed above. All the evidence in the administrative file points to a time-sharing arrangement for the use of land which you have purchased so that your Members may hunt and fish. From the information furnished, any social commingling among your limited membership appears minimal, at best, in the context of your activities.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(7) of the Code and you must file federal income tax returns.

[REDACTED]

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201.

When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

Internal Revenue Service
[REDACTED]
[REDACTED]

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

[REDACTED]
[REDACTED]
Manager, Exempt Organizations
[REDACTED]

Code	Initiator	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer
Surname	[REDACTED]	[REDACTED]				
Date	[REDACTED]	[REDACTED]				